

**EXECUTIVE SECRETARIAT**  
**ROUTING SLIP**

TO:		ACTION	INFO	DATE	INITIAL
1	DCI		X		
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8	DDS&T				
9	Chm/NIC				
10	GC				
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SUSPENSE      3 Apr 86  
Date

Remarks

To 5: Please handle as appropriate and get back to the DCI on (a) additional reaction to theory, and (b) NIO/ECON.

Executive Secretary

19 Mar 86

Date

3637 (10-81)

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Executive Registry

86- 1165

19 March 1986

MEMORANDUM FOR: Deputy Director for Intelligence

FROM: Director of Central Intelligence

25X1

SUBJECT: Soviet Financial Practices

I think there is something to this (see attached articles). I had [redacted] and his people take an earlier look at it, but they didn't think much of the theory. We ought to see what some bankers like [redacted] think about it. Roger Robinson was the chief NSC economic staffer until he left about six months ago. I don't know what he is doing now, but he could be a possibility for NIO/Economics.

25X1



William J. Casey

25X1

~~SECRET~~

THE WALL STREET JOURNAL MONDAY, MARCH 10, 1986

# Financing the Soviet Union

By ROGER W. ROBINSON JR.

Hasn't it struck most Western policy makers as odd that the Soviet Union, with a total annual hard-currency income of only about \$32 billion from all sources (including arms sales), can sustain a global empire? More specifically, how does the U.S.S.R. support such a vast array of third-country commitments—many of which must be financed by hard currency—with annual earnings equivalent to about one-third of Exxon's annual revenue for 1985? Untied and unobserved Western financial flows to the Warsaw Pact countries are, in my view, a principal avenue by which the West contributes to the Soviet Union's ability to maintain and expand its costly global commitments.

In his novel "The Honorable Schoolboy," John LeCarre offered some sound advice concerning financial flows to potential adversaries, which was embodied in three words: "Follow the money." That is exactly what I recommend we do.

In this connection, I've often been curious why I've never seen a security-oriented cash-flow analysis of the U.S.S.R.—a page divided down the middle with "sources" of hard currency on the left side (for example, oil and natural-gas exports and the sales of arms, gold, diamonds, etc.) and "uses" of hard currency on the right side (such as imports from the West, technology theft, the underwriting of client states, KGB operations and other expenditures). My own guess is that a detailed security cash-flow analysis of this kind would show a formidable annual hard-currency shortfall that presumably has to be financed through Western borrowings.

## Rather Hidden Source

Declining Soviet oil production and plummeting prices for both oil and natural gas—which constitute approximately two-thirds of the U.S.S.R.'s total annual hard-currency earnings structure—should result in an even more active Soviet presence on the world credit markets than the roughly \$4.5 billion in new credits observed in 1985. The fact is that the level of Soviet indebtedness remained largely unchanged between 1979 and 1984 even though the U.S.S.R.'s hard-currency needs apparently grew significantly. I believe this discrepancy can be, at least in part, explained by substantial Soviet reliance on a rather hidden borrowing source in Western financial markets.

This less visible borrowing activity takes place in the vast and amorphous interbank market where the Soviet Union has been a major player for many years. The interbank market is global in scope and has been formed by the established practice among the world's banks of depos-

on excess cash. The London Interbank Offered Rate (Libor) serves as a benchmark rate at which these deposits are offered to prime potential borrowers and usually floats at roughly one percentage point below the U.S. prime rate. Interbank transactions can either be arranged by a money broker or directly between banks. A typical transaction might have bid and offer rates of 7½% and 8%, respectively, with the higher rate representing the price at which a bank would offer or sell deposits to another bank. Prior to concluding an interbank transaction, the bank offering the funds will check the credit limit for the particular bank taking the funds, as well as the "country exposure limit" for the country in which the bank is based. It is not in all cases standard practice to check the "country exposure limit" for the coun-

try (such as the Soviet Union) that may own the "taking" bank.

The six Soviet-owned banks located in the West, along with their branches, have been major beneficiaries of this global flow of interbank funds. The largest Soviet-owned banks in the West include Banque Commerciale pour l'Europe du Nord, or Eurobank, in Paris, Moscow Narodney Bank, London (which often serves as the coordinating point for other Soviet banking institutions in the West), and Ost-West Handelsbank in Frankfurt. Other 100% Soviet-owned banking institutions are in Luxembourg, Zurich and Vienna. The Soviets go to some lengths to obscure their complete ownership of these institutions. For example, these banks are incorporated under the laws of the countries in which they are based, have foreign nationals in management positions, have what appears to be a diverse group of shareholders, and even maintain offices in Moscow that are similar to those of Western banks.

These Soviet banks engage in other banking activities outside the interbank market and even place some of their own deposits with major Western banks. This does not, however, offset the enormous advantage to the Soviets of having access to this kind of oversized reserve checking account at an interest rate that is substantially below the U.S. prime rate and that can be used at their sole discretion. Similar to a cash-reserve bank line to bridge shortages of cash in a regular checking account, interbank deposits provide the Soviets with needed liquidity on the margin to meet their pressing cash requirements. Access to these Western deposits also per-

mits the Soviets to avoid more expensive and visible forms of Western financing. After all, why should the U.S.S.R. step up its modest use of bankers' acceptances or go more often to the syndicated loan market when it can tap a largely invisible pool of Western deposits at interest rates well below U.S. prime? (Interest rates on most loans to the U.S.S.R. are at some fraction of one percentage point above the LIBOR rate and are still below U.S. prime.)

It is very difficult to estimate the precise amount of such Western funds on deposit with the Soviet Bank for Foreign Trade, the Comecon banks, the State Bank of the U.S.S.R., and Soviet-owned banks in the West. Nevertheless, as the Soviets maintain correspondent banking relations with virtually every sizable banking institution in the world, a ballpark estimate of

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rates well below U.S. prime?*

Western deposits with Soviet-owned banks in the West would be roughly \$5 billion. I would estimate that several billion dollars more in Western deposits have been attracted directly by the Soviet Bank for Foreign Trade and the Comecon banks. Individual East European banks also enjoy the same favorable access to this untied, low-cost financing source. Although these deposits must eventually be repaid, similar to loans, they still represent a major reservoir of cheap money.

Congress, in close coordination with the Reagan administration, can play an important role in examining the practice of untied, or so-called balance-of-payments, lending to potential adversaries and understanding the extent to which the Soviets rely on interbank deposits. Certain principles or guidelines should also be considered for voluntary adoption by the Western banking community if they have not already been instituted.

Specifically, each loan to a potential adversary should have an identified and verifiable purpose—be it an equipment purchase, a specific project (with loan draw-downs calibrated to project expenditures) or a short-term commodity transaction such as a grain purchase. Every loan should have a maturity that is strictly matched against the duration of the underlying transaction. For example, a grain transaction should be financed with a maximum loan maturity of 180 days, rather than the three years that would de facto provide the Soviets with 2½ years of cash for their discretionary use. Finally, U.S. banks should aggregate their interbank deposit exposure to all Soviet-owned entities

and periodically report these aggregate exposures to U.S. bank regulators, if they are not already doing so. The same practices should be applied regarding East European banks.

I am not arguing for the discontinuation of interbank activity with the U.S.S.R.—only that specific information be developed on the amounts and the proper use and maturity of such deposits. These proposed principles to govern financial flows to potential adversaries are prudent from a commercial as well as security perspective and, therefore, should not present major problems for Western banks.

The administration should also urge our allies, through the Organization for Economic Cooperation and Development, to monitor the implementation of similar guidelines. In the event that the administration is disappointed by the lack of allied cooperation, more information should be gathered to determine the respective levels of allied involvement in untied, non-transparent financial flows to potential adversaries and what, if anything, should be done about them. Generally, U.S. banks are more conservative and disciplined in their lending policies than their European and Japanese counterparts and maintain lower credit exposures.

### Cannot Avert Our Eyes

There don't have to be any "losers" in the West as a result of these policy recommendations. Legitimate, nonstrategic trade can go forward and expand; the U.S. can continue to streamline and expedite its export-licensing procedures and trim the list of controlled technologies (Cocom), where indicated, to ensure enhanced U.S. export competitiveness; Western loans can continue to support specific trade transactions and projects; and let's hope incentives for greater Soviet geopolitical cooperation can be created through expanded East-West economic and commercial relations. We simply cannot avert our eyes from those financial practices that are potentially harmful to our long-term security interests; nor can we sidestep the need to develop a more comprehensive picture of how the Soviet Union funds itself and its global activities.

Finally, it is imperative that we successfully come to terms with the enormous contribution the West is making to the economic and financial vitality of the Soviet Union and its client states, especially at a time of budget-related austerity at home.

*Mr. Robinson is president of RWR Inc., a Washington-based consulting firm. From 1982 to 1985 he was senior director for international economic affairs at the National Security Council. This is adapted from a talk given early last month at the Heritage Foundation.*

THE JOURNAL OF COMMERCE  
Wednesday, 5 March 1986

# Soviet Bank Deposits Questioned

By RICHARD LAWRENCE

*Journal of Commerce Staff*

WASHINGTON — Western banks may be unwittingly helping finance subversive Soviet activities in the West, a former Reagan administration aide suggested.

Soviet banks, Roger Robinson, a recent National Security Council adviser, said, have access to perhaps as much as \$10 billion in Western bank funds through inter-bank deposits.

He likened these deposits to a "kind of oversized reserve checking account (for the Soviet Union) at an interest rate below the U.S. prime rate." The Soviets, he said, can use the funds "at their sole discretion."

Inter-bank deposits, whereby banks place short-term deposits with one another, help facilitate the flow of funds and earn banks income on excess cash. The deposits usually are made at the London Interbank Offering Rate, generally about 1% below the New York prime rate.

Mr. Robinson, now president of RWR Inc., a Washington consulting firm, estimates that western banks have about \$5 billion on deposit with Soviet-owned banks in the West, which include Moscow Narodny Bank in London, Ost-West Handelsbank in Frankfurt, and Banque Commerciale pour l'Europe du Nord, Paris.

He further estimates that "several billion dollars more in western deposits" are with the Soviet Bank for Foreign Trade and Soviet-dominated Comecon banks.

The Soviet Union, Mr. Robinson said in a speech at the Heritage Foundation, appears to be tapping these "rather hidden" funds to help underwrite Cuba and other client states, KGB/GRU operations, technology theft and other international activities.

Soviet reliance on inter-bank deposits, he sug-

gested, may rise further, as its hard currency export earnings — about two-thirds of them in oil and gas — start to dwindle.

Mr. Robinson urged the administration and Congress to examine the whole range of "untied" western credits to the Soviets, including the Soviet Union's use of inter-bank deposits.

"We simply cannot avert our eyes from those economic and financial practices deleterious to our long-term security interests; nor can we sidestep the need to develop a more comprehensive picture of how the Soviet Union funds itself and its global activities," he said.

Western banks, Mr. Robinson suggested, should consider voluntary guidelines for lending to the Soviet Union. Loans, he said, should be committed only for an "identifiable and verifiable purpose" and maturities should be "strictly matched against the duration of the underlying transaction."

U.S. banks, he said, also should aggregate their inter-bank deposit exposures to all Soviet banks and report periodically to federal regulators. Other western countries should be persuaded to adopt similar practices, he said.

Mr. Robinson's remarks came as the Senate Banking Committee may be about to vote on a bill to give the president standby authority to bar all financial transactions with the Soviet Union. The Reagan administration opposes the bill, but Banking Committee Chairman Jake Garn, R-Utah, intends to press ahead with it.

Another bill, introduced this week in Congress, would bar Soviet or other East Bloc citizens from buying a U.S. bank. Moscow Narodny Bank in the mid-1970s tried covertly to acquire several California banks.

## Soviet Plan Falls Short of Goals

By ALBERT AXEBANK

Journal of Commerce Special

MOSCOW — Prime Minister Nikolai Ryzhkov admitted that the five-year national economic development plan that just ended was a partial failure.

Mr. Ryzhkov, speaking at the Party Congress here, put the blame on miscalculations of ministries, shortsightedness of some managers, and on other "unfavorable tendencies."

However, he said that a good deal was accomplished in the 1981-1985 plan period, although "the assignments of the plan were not fully attained."

Mr. Ryzhkov, a Politburo member, also spoke at length about the ambitious new 12th five-year plan (1986-1990) including the guidelines ending in the year 2000. He cited the need for a "profound restructuring of the Soviet economy."

He said that in the course of the next 15 years, it is planned to double the national income and the industrial output.

Mr. Ryzhkov mentioned the

breaking down of all the barriers to swift economic and technological progress.

Western analysts call the guidelines for the new plan and for the next 15 years perhaps overly ambitious. Some of them question how such grand targets can be met when the country's industry now has trouble turning out a really good shovel, or a first-rate socket wrench.

The prime minister said a characteristic feature of the new plan was the emphasis on retooling and modernizing the existing production facilities.

He said the economic guidelines envisage increasing the labor productivity 20%-23% as against 16.5%-16.5% in the past five-year plan. More economical use also would be made of fuel and raw materials. He also said capital investments would be substantially greater in the new plan, some US\$235 billion as compared to US\$175 billion for the previous plan.

Mr. Ryzhkov said there would

be an 80% growth of investments in the "engineering complex" under the new plan. He did not further elaborate.

Speaking about nuclear power generation, he said that by the end of the new plan nuclear power stations would nearly double their share of power production and account for more than 20% of the total amount produced.

The prime minister said that in the field of agriculture, it was planned to bring the output of grain up to as high as 255 million metric tons annually.

Western sources note that this clearly ambitious target would be more than 50 million metric tons above the present levels.

Mr. Ryzhkov said the party was striving to eliminate the barriers standing in the way of scientific and technological progress. "Although we possess noteworthy R&D, we often lag behind in the development of progressive technologies," he said. This situation must be changed, he added.

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